

An ideal stocking filler for patient investors

4th December 2019

What do UK investors most want for Xmas? Well considering the hand-wringing caused by the US/China trade spat, UK General Election and Brexit 'limbo', we suspect greater clarity would be towards the top of Santa's list.

The good news is that we think much of this uncertainty could be resolved over the next few months, providing not only a welcome boost to capital investment - but also a lift to specialist plant hire firms like Vp, who posted **resilient H1'20 numbers** this morning.

On track to deliver FY20 PBTA forecasts of £49.6m

Here **adjusted EBITDA, PBTA and EPS** (see below, pre IFRS 16) were **broadly flat YoY** at £51.8m (+0.4%), £25.9m (+0.3%) and 52.5p (+0.2%) respectively, despite strong comparatives and turnover easing -3.4% to £186.6m. The latter reflecting **softer conditions in commercial construction & civil engineering** (centred around London & the South East), and exacerbated by completion of the 5-year Water (AMP 6) & Rail (CP5) programs. Albeit equally **offset by higher EBIT margins** (15.2% vs 14.6% LY) thanks to Brandon synergies, tight cost control and improving demand at Airpac Bukom (oil & gas), where new fleet has been ordered.

Robust H1'20 numbers

£'000s March yearend	Act H1'19	Act H1'20	%	Act H2'19	Est H2'20	%	Act FY19	Est FY20	%
UK sales	175,338	170,016	-3.0%	174,992	180,234	3.0%	350,330	350,250	0.0%
International	17,873	16,569	-7.3%	14,627	16,181	10.6%	32,500	32,750	0.8%
Group revenues	193,211	186,585	-3.4%	189,619	196,415	3.6%	382,830	383,000	0.0%
Group EBITDA	51,629	51,840	0.4%	49,710	51,629	3.9%	101,339	103,959	2.6%
EBIT % margin	26.7%	27.8%		26.2%	26.3%		26.5%	27.1%	
EBITDA (post IFRS 16)		64,782			65,061			129,843	
UK	26,912	27,245	1.2%	22,959	24,697	7.6%	49,871	51,942	4.2%
International	1,266	1,070	-15.5%	434	1,157	166.6%	1,700	2,227	31.0%
Group EBITA	28,178	28,315	0.5%	23,393	25,854	10.5%	51,571	54,169	5.0%
EBITA (post IFRS 16)		30,250			27,789			58,039	
UK	15.3%	16.0%		13.1%	13.7%		14.2%	14.8%	
International	7.1%	6.5%		3.0%	7.2%		5.2%	6.8%	
EBIT % margin	14.6%	15.2%		12.3%	13.2%		13.5%	14.1%	
Interest	-2,325	-2,383	2.5%	-2,417	-2,217	-8.3%	-4,742	-4,600	-3.0%
PBTA	25,853	25,932	0.3%	20,976	23,637	12.7%	46,829	49,569	5.9%
PBTA (post IFRS16)		25,772			23,477			49,249	
Adj EPS - pre IFRS16	52.3p	52.5p	0.2%	42.8p	47.6p	11.2%	95.1p	100.1p	5.2%
Adj EPS - post IFRS16		52.1p			47.3p			99.4p	
Dividend	8.2p	8.45p	3.0%	22.0p	22.7p	3.0%	30.2p	31.1p	3.0%
Net debt (pre IFRS 16)	-188,236	-183,746	-2.4%	-168,100	-163,500	-2.7%	-168,100	-163,500	-2.7%
Net debt : EBITDA							1.7	1.6	
Group ROCE	15.6%	14.5%					14.5%	14.7%	

Source: Equity Development

Elsewhere, both **UK infrastructure & housebuilding held up well**, mirroring near-record employment, low borrowing costs, good mortgage availability and the popular Help to Buy scheme. Meanwhile overseas, TR Pty (test & measurement) delivered solid results in Malaysia & Singapore, but experienced tougher trading in Australia.

Company Data

EPIC	LSE: VP.
Price (last close)	890p
52 week Hi/Lo	1,060p/690p
Market cap	£357m
Est. Mar'20 net debt	£163.5m
Share count	40.154m
ED valuation/share	£10.75
Daily volume	20,000

Share Price, p



Source: Share Cast

Description

Vp is a specialist rental business providing equipment and services to a wide range of markets including civil engineering, rail, oil/gas exploration, construction, outdoor events and industry, primarily within the UK (91% H1'20 turnover), but also from overseas.

In terms of sector split: 38.7% H1'20 sales came from infrastructure, 39.8% construction, 9.0% housing building, 6.7% oil & gas and 5.8% other.

Member of FTSE SmallCap Index.

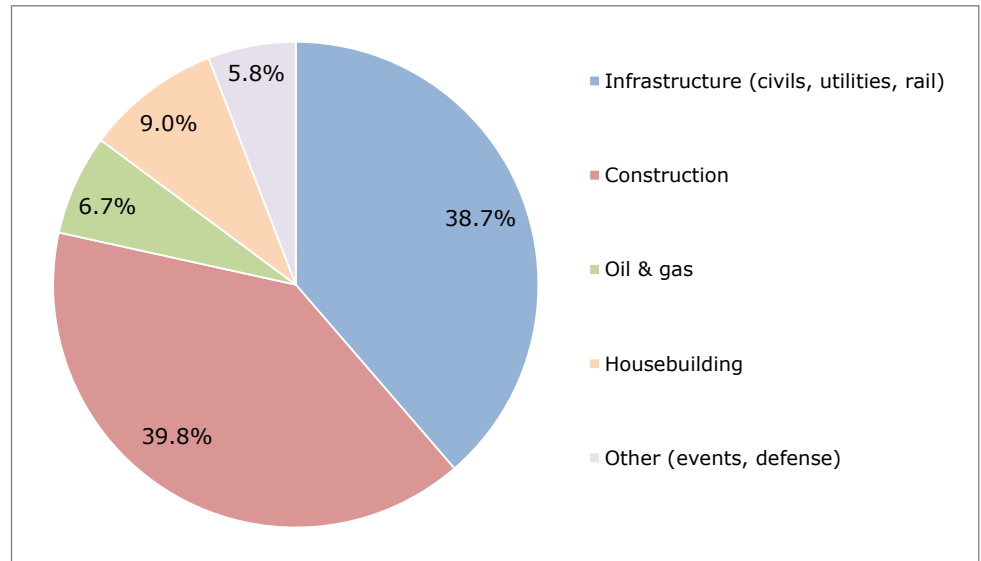
Next news: Trading update April 2020

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H1'20 revenue (£186.6m) split by market

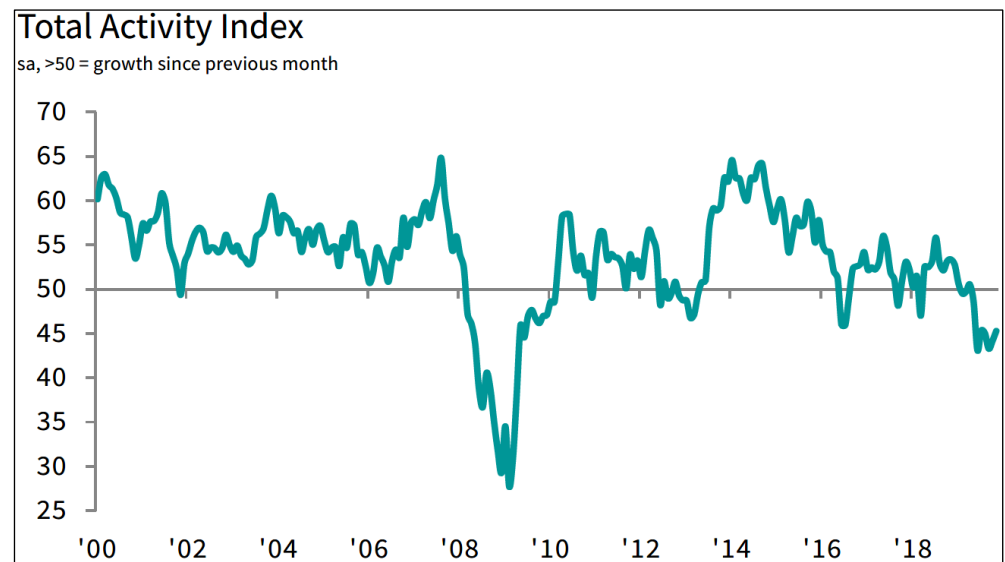


Source: Equity Development

Resilient 1st half despite macro headwinds

Overall we believe these are commendable results, illustrating Vp’s **downside resilience**, **differentiated service offering** and **focus on specialist equipment**. Especially in light of yesterday’s muted IHS Markit/CIPS UK Construction report (see below), which saw activity levels fall to 45.2 in November (<50 implies contraction) – with a “*sharp drop off in new work*” due to “*domestic political uncertainty, indecision among clients and unusually wet weather*”.

UK Construction PMI (purchasing managers’ index)

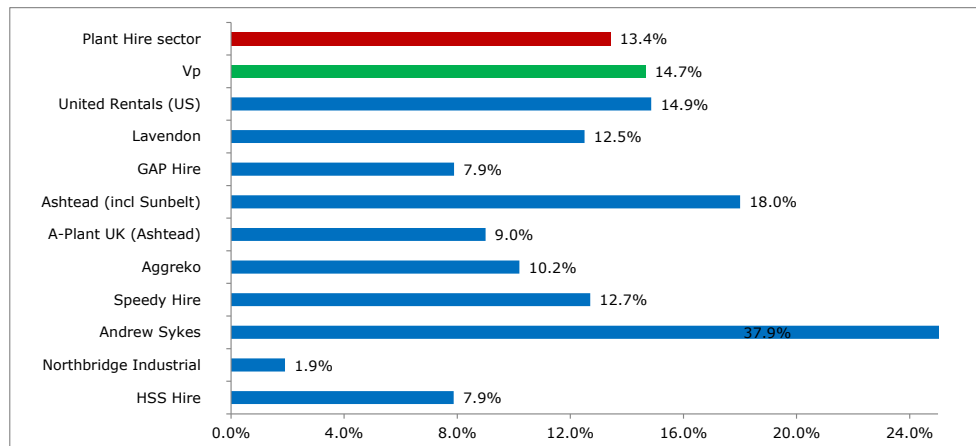


Source: IHS Markit December 3rd 2019

Healthy ROCE and set to improve further

What’s more, **H1 ROCE came in at a healthy 14.5%** (see below), which – although slightly below the Board’s own stretching 15% target - was a function of the mix effect of combining the £69.2m Brandon acquisition (Est 10% ROCE) with the existing business (16%).

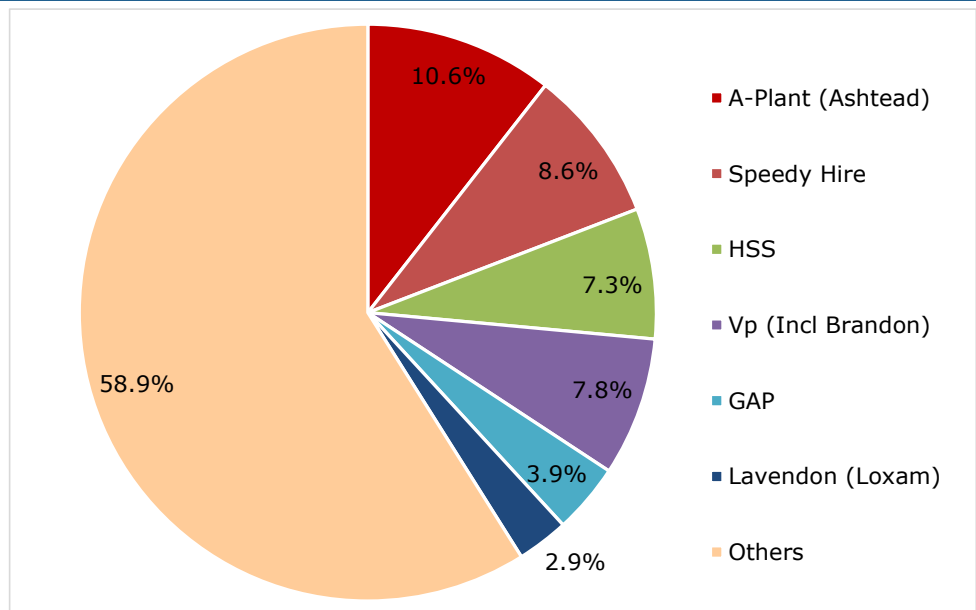
Current Year (CY) ROCE across sector



Source: Equity Development

Besides, the 14.5% exceeds most of Vp’s rivals anyway across the circa £4.5bn UK tool/plant hire & related services market (see below).

UK equipment hire market shares

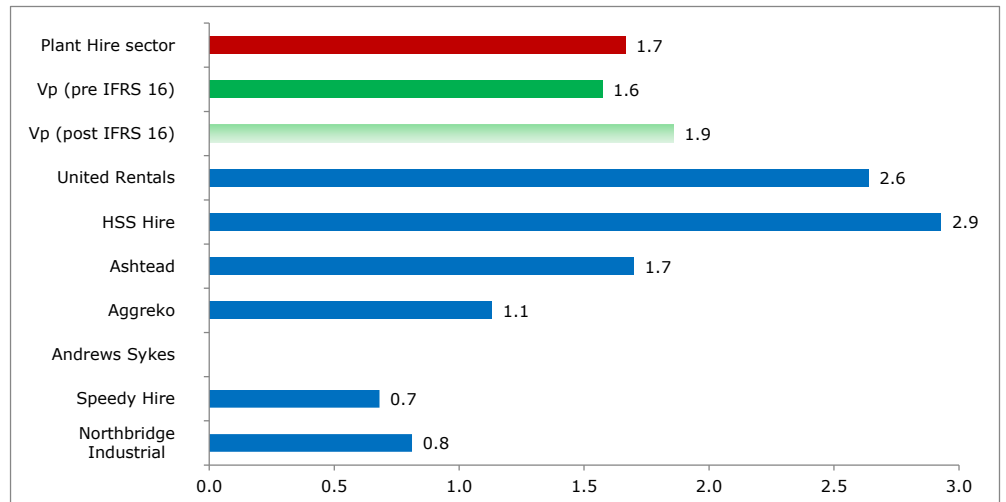


Source: Equity Development

Prudently geared & generating robust cashflows

In terms of the balance sheet, **net debt** (pre IFRS 16) **closed Sept’19 at £183.7m**, up £15.6m from Mar’19 (£168.1m), after absorbing restructuring payments (ie provided for at y/e), dividends (£8.7m), the Sandhurst acquisition (£3.3m) and a rise in debtor days (66 vs 58 LY), partly compensated by less fleet capex at £18.6m (net) vs £29.3m LY. Going forward, **net debt:EBITDA** (pre IFRS16) **is anticipated to decline to 1.6x by Mar’20** from 1.7x in FY19.

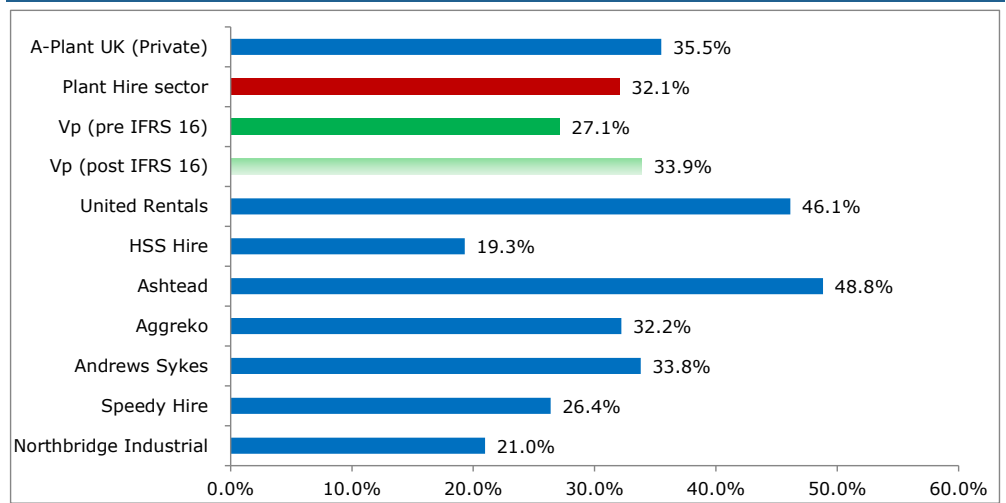
CY Net debt : EBITDA



Source: Equity Development (arithmetic average for sector).

Similarly, as the final synergies from the Brandon acquisition (ED Est of >£2.5m annualised) flow through over the next 6 months or so, **EBITDA/EBIT margins** (see below) **and ROCE should further expand**, alongside another tick down in financial gearing.

CY % EBITDA margins vs peers

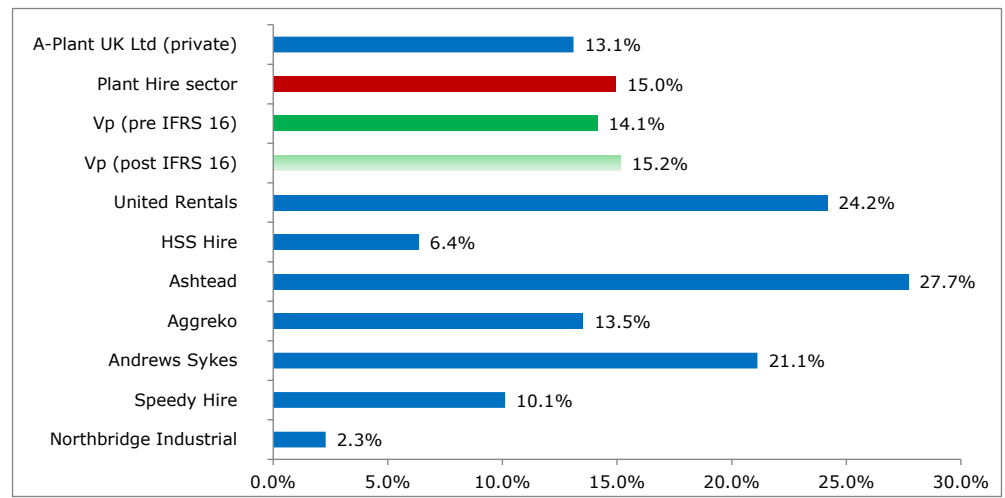


Source: Equity Development (arithmetic average for sector)

Pre-IFRS 16 numbers are more representative

By the way, Vp (like all other listed stocks) is presently mid-stream in implementing IFRS 16 - ie relating to the treatment 'operating leases'. For the purposes of interpretation, **we suggest investors focus on the 'pre-IFRS 16' figures** (ie shown in solid green), since the new accounting standard arbitrarily capitalises leases. In turn, artificially inflating assets and liabilities on the balance sheet that have little resemblance to the commercial reality of agreed contracts. For instance, Vp now has **£77.8m of 'non-interest-bearing lease liabilities'** - split property (£55.2m eg offices/depots), equipment (£10.9m eg plant) and vehicles (£11.6m eg service vans & delivery trucks) - where interest and depreciation is hypothetically charged to the P&L.

CY VP's % EBIT margins vs peers

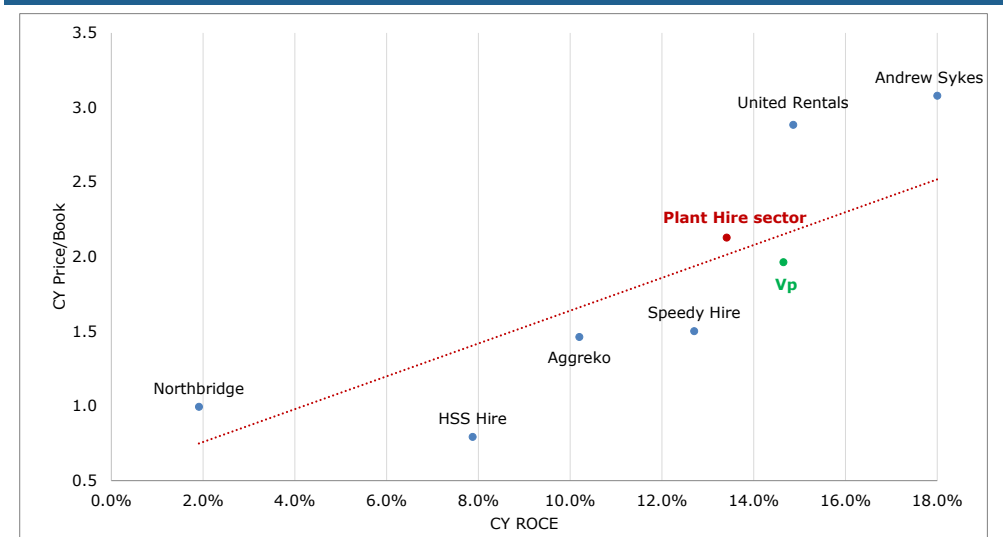


Source: Equity Development (arithmetic average for sector)

Fine, but what about the outlook?

In the short term, today's more challenging backdrop is likely to continue until (at least) next Spring, but conditions should improve thereafter. Plus, **we are confident about our FY20 PBTA** (£49.6m) & **EPS forecasts** (100.1p), and **cautiously optimistic about next year** - given the possibility of a 'capex catchup', as delayed construction, infrastructure & housebuilding projects are brought on stream (nb not factored into our estimates).

Current Year ROCE vs Price: Book

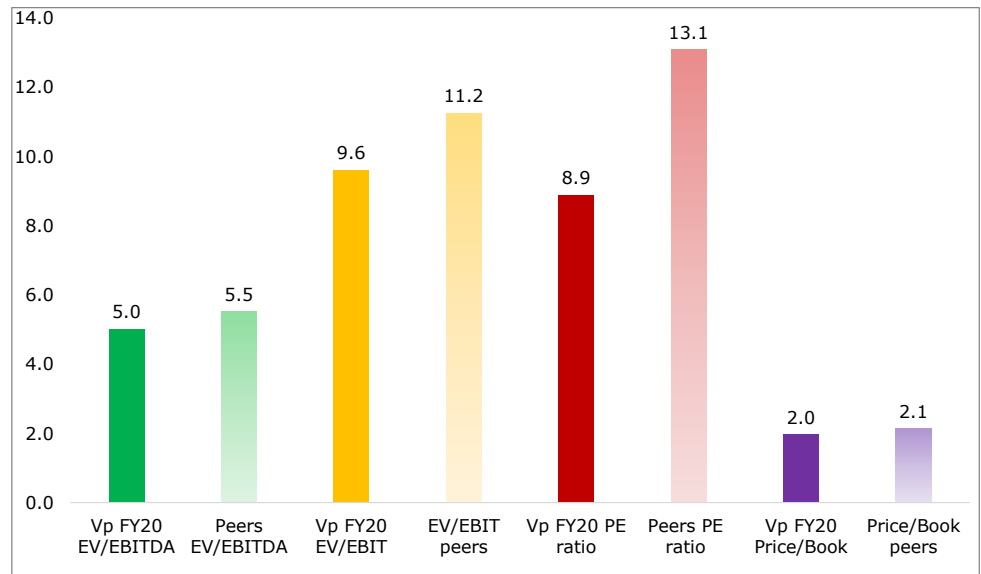


Source: Equity Development

Valuation asymmetrically biased to the upside

With regards to valuation, **we calculate the stock to be worth £10.75/share** - potentially offering >20% upside to patient investors - and see real upside in the event there is a sector upswing (re 'mini Boris Boom'), perhaps even in late 2020 once the Brexit induced logjam has cleared.

CY summary multiples vs peers (pre IFRS16)



Source: Equity Development – closing prices as at 26th November 2018

Possible 'mini Boris boom' next year

Chairman Jeremy Pilkington commenting: ***"The Group made good progress in H1'20 against a subdued market backdrop. Despite the ongoing political and economic uncertainty in the UK, our focus on quality of earnings has delivered enhanced operating margins during the period."***

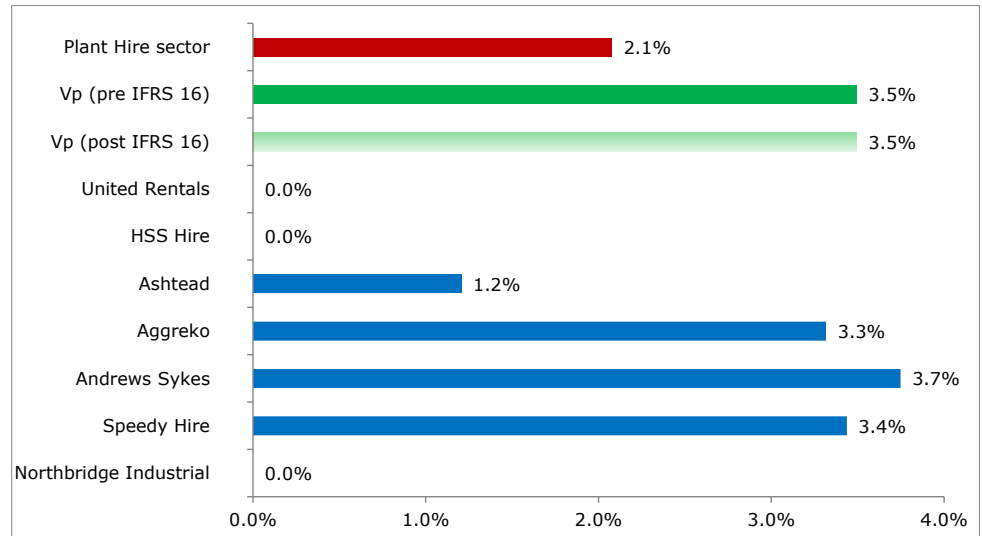
Trading continues in line with the Board's expectations and we remain confident of a positive full year outcome."

Moreover further out, there is no a shortage civils demand either. Not least in power generation (renewables, Hinkley Point C), rail (electrification, track upgrades, Crossrail 2, HS2), water (London's super sewer, national grid), airport (eg Heathrow 3rd runway), road (electric vehicles), residential property and 5G wireless / broadband.

Dividend nudged up 3%, offering 3.5% yield

Shareholders are set to receive a welcome Christmas gift too, with the **interim dividend lifted 3% to 8.45p** - payable on 17 January 2020 (ex-div Thursday 13 December) - representing a **prospective yield of 3.5%** (see below).

CY dividend yield vs peers



Source: Equity Development

CMA investigation should (hopefully) be resolved soon

Lastly, it is worth mentioning the ongoing Competition and Markets Authority (CMA) investigation. Here, the CMA has provisionally concluded that 3 major suppliers of groundwork products – including Vp’s Groundforce unit - were involved in suspected anti-competitive behaviour.

The findings are provisional at this stage, and do not mean that any company breached competition law. As such, it is impossible to accurately assess the likely costs associated with this enquiry. Nonetheless, in line with accounting standard IAS 37, Vp included an exceptional charge of £4.5m within its FY19 accounts.

The figure is in the arithmetic midpoint of a range of possible outcomes (£0m to £9.0m) that the Board have calculated based upon previous cases and CMA published guidance – importantly though, without any admission of blame. Hence, whilst the case is undoubtedly something to watch, **we guess it won’t ultimately end up being material in the context of the group’s £357m marketcap.**

Forecasts (£'000s)

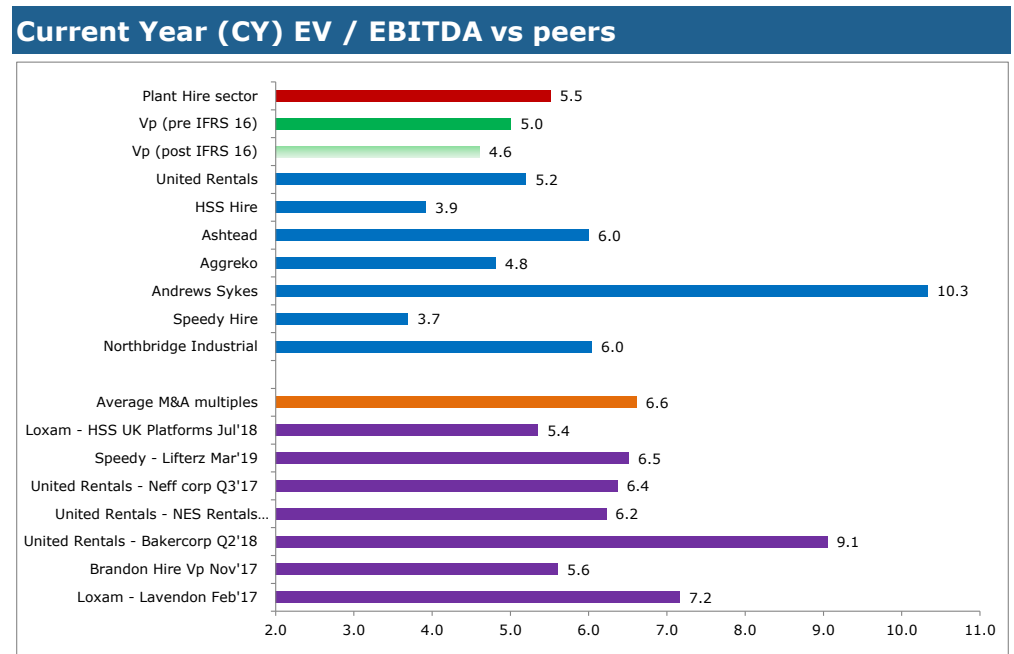
Vp (March year end)	2015 Act £'000s	2016 Act £'000s	2017 Act £'000s	2018 Act £'000s	2019 Act £'000s	2020 Est £'000s	2021 Est £'000s	2022 Est £'000s	2023 Est £'000s
Turnover									
UK	184,142	193,555	220,015	271,989	350,330	350,250	357,255	367,973	379,012
International	21,460	15,191	28,725	31,650	32,500	32,750	33,405	34,741	36,131
Total	205,602	208,746	248,740	303,639	382,830	383,000	390,660	402,714	415,143
% growth	12.3%	1.5%	19.2%	22.1%	26.1%	0.0%	2.0%	3.1%	3.1%
UK		5.1%	13.7%	23.6%	28.8%	0.0%	2.0%	3.0%	3.0%
International		-29.2%	89.1%	10.2%	2.7%	0.8%	2.0%	4.0%	4.0%
EBITDA	53,803	59,266	71,238	84,337	101,339	103,959	106,811	110,675	114,652
% Margin	26.2%	28.4%	28.6%	27.8%	26.5%	27.1%	27.3%	27.5%	27.6%
EBITDA (post IFRS16)						129,843	132,695	136,559	140,536
Adjusted EBIT									
UK	26,027	30,659	35,871	43,001	49,871	51,942	53,022	54,769	56,569
International	2,753	1,232	1,886	1,017	1,700	2,227	3,003	3,553	4,114
Total	28,780	31,891	37,757	44,018	51,571	54,169	56,025	58,322	60,683
EBIT (post IFRS16)						58,039	59,119	60,866	62,666
% Margin	14.0%	15.3%	15.2%	14.5%	13.5%	14.1%	14.3%	14.5%	14.6%
UK	14.1%	15.8%	16.3%	15.8%	14.2%	14.8%	14.8%	14.9%	14.9%
International	12.8%	8.1%	6.6%	3.2%	5.2%	6.8%	9.0%	10.2%	11.4%
Interest charge (pre IFRS 16)	-2,023	-2,093	-2,906	-3,421	-4,742	-4,600	-4,400	-4,100	-3,800
Adjusted PBT (pre amortisation)	26,757	29,798	34,851	40,597	46,829	49,569	51,625	54,222	56,883
PBT (post IFRS16)						49,249	51,305	53,902	56,563
Adjusted earnings	21,201	24,226	27,262	33,520	37,677	39,655	41,300	43,378	45,506
Adjusted Basic EPS (p) - pre IFRS 16	54.4	62.2	69.5	84.9	95.1	100.1	103.7	108.4	113.1
EPS growth rate	29.7%	14.3%	11.7%	22.1%	12.0%	5.2%	3.6%	4.5%	4.4%
Adjusted EPS diluted	50.2	59.0	67.6	83.9	92.2	97.0	0.0	0.0	0.0
Basic EPS (post IFRS16)						99.4	103.1	107.7	112.5
Dividend (pence)	16.5	18.9	22.0	26.0	30.2	31.1	32.2	33.7	35.2
Dividend growth	17.9%	14.2%	16.7%	18.2%	16.2%	3.0%	3.6%	4.5%	4.4%
Valuation benchmarks									
P/E ratio (pre IFRS 16)	16.3	14.3	12.8	10.5	9.4	8.9	8.6	8.2	7.9
P/E ratio (post IFRS 16)						9.0	8.6	8.3	7.9
EV/Sales	2.5	2.5	2.1	1.7	1.4	1.4	1.3	1.3	1.3
EV/EBITDA (pre IFRS 16)	9.7	8.8	7.3	6.2	5.1	5.0	4.9	4.7	4.5
EV/EBITDA (post IFRS 16)						4.6	4.5	4.4	4.3
EV/EBITA (pre IFRS 16)	18.1	16.3	13.8	11.8	10.1	9.6	9.3	8.9	8.6
EV/EBITA (post IFRS 16)						10.3	10.1	9.8	9.6
PEG ratio	0.5	1.0	1.1	0.5	0.8	1.7	2.4	1.8	1.8
Dividend yield	1.9%	2.1%	2.5%	2.9%	3.4%	3.5%	3.6%	3.8%	4.0%
Dividend cover	3.3	3.3	3.2	3.3	3.2	3.2	3.2	3.2	3.2
Corporate tax rate	-20.8%	-18.7%	-21.8%	-17.4%	-19.5%	-20.0%	-20.0%	-20.0%	-20.0%
Net debt / EBITDA (pre IFRS 16)	1.2	1.5	1.4	2.0	1.7	1.6	1.3	1.0	0.8
Return on average capital employed	16.2%	16.3%	16.0%	14.8%	14.5%	14.7%	14.8%	15.0%	15.1%
Net cash/(debt) - pre IFRS16	-66,764	-86,134	-98,933	-179,172	-168,100	-163,500	-138,633	-112,707	-86,638
Fleet capital expenditure (gross)	49,300	45,900	57,600	64,900	63,800	60,000	63,000	65,000	68,000
Investment as % sales	24.0%	22.0%	23.2%	21.4%	16.7%	15.7%	16.1%	16.1%	16.4%
Reported sharecount Ks (net Treasury)	38,940	38,942	39,215	39,476	39,603	39,630	39,828	40,027	40,227
Shareprice (p)	890								

Source: Equity Development

Key risks

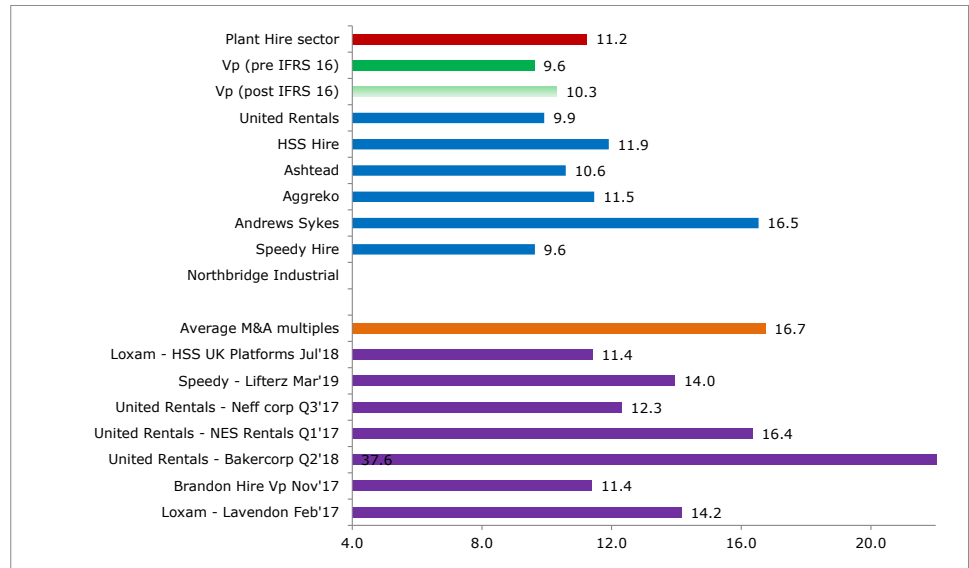
- In light of Vp's operational gearing, if the economy stalled then this could impact earnings as costs are predominantly fixed. That said, investment in the hire fleet can be flexed as conditions change as occurred during the 2008/9 recession.
- Competitive pricing pressures and higher interest rates that could lift funding costs, yet 40% of gross debt is fixed.
- Acquisition integration, albeit the management's track record to date has been good.
- 50.26% of the equity is owned by a number of trusts connected to Exec-Chairman Jeremy Pilkington (re possible hypothetical impact on minority interests), although this should also help ensure the group is run to maximise shareholder value.

Appendix - Sector valuation metrics and KPIs



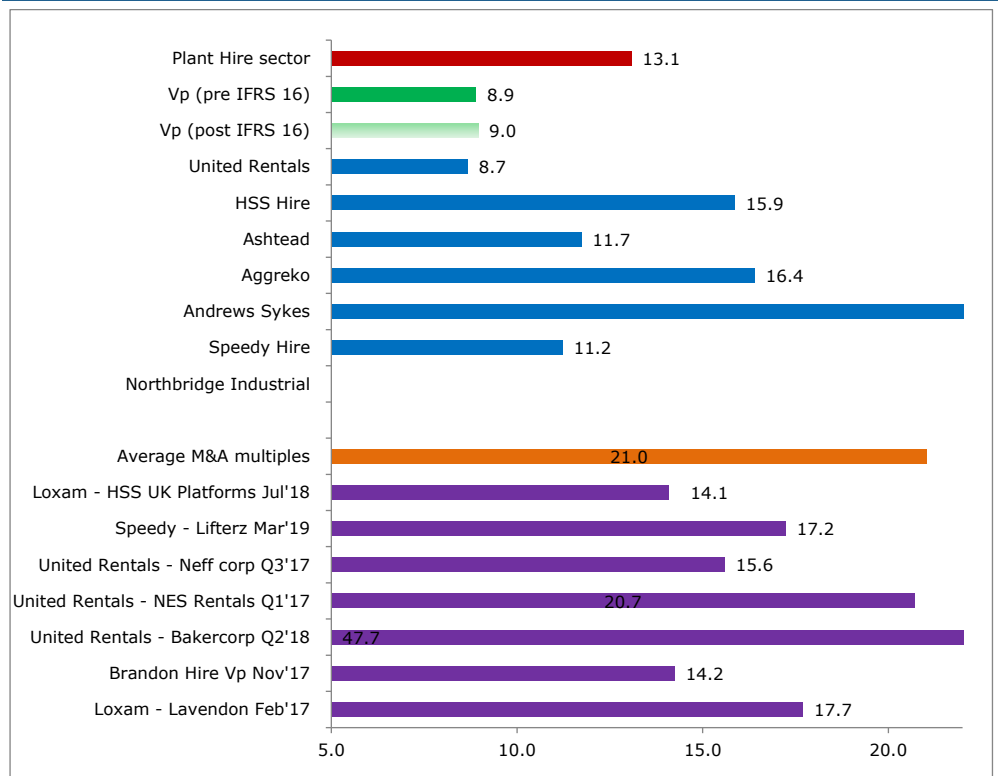
Source: Equity Development, arithmetic average for sector

CY EV / EBIT vs peers



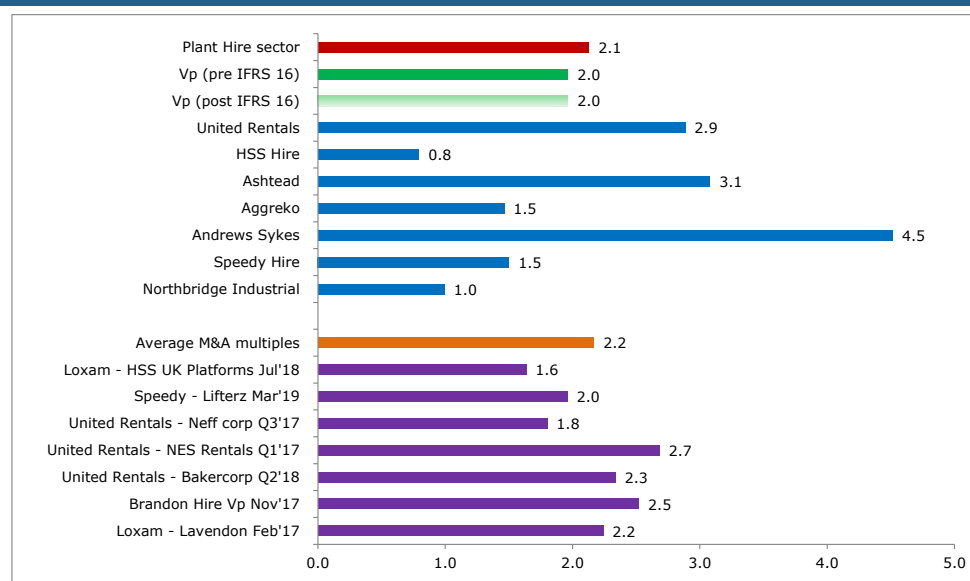
Source: Equity Development, arithmetic average for sector

CY PER vs peers



Source: Equity Development, arithmetic average for sector

CY Price : Book vs peers



Source: Equity Development, arithmetic average for sector

Market capitalisation of sector

	Shareprice	Mrk Cap (Ms)	CY net cash / (debt) Ms	Enterprise Value (Ms)
Northbridge Industrial	128p	£36.1	-£5.6	£41.7
Speedy Hire	64p	£336	-£76	£412
Andrews Sykes	635p	£268	£20	£248
Aggreko	817p	£2,083	-£640	£2,723
Ashtead	2,280p	£10,944	-£4,586	£15,530
HSS Hire	37p	£63.0	-£186.0	£249.0
United Rentals	\$148	£11,026	-£11,353	£22,379
Vp	890p	£357	-£164	£521

Source: Equity Development



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